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Report On Business®

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Economy Declines Further: PMI Falls to 48.8%

Price Index Declines: Lowest Since April 1986

Analysis by the National Association of Purchasing Management Business Survey Committee; chair, Robert J. Bretz, C.P.M., director of materials management, Pitney Bowes, Inc.

June Report

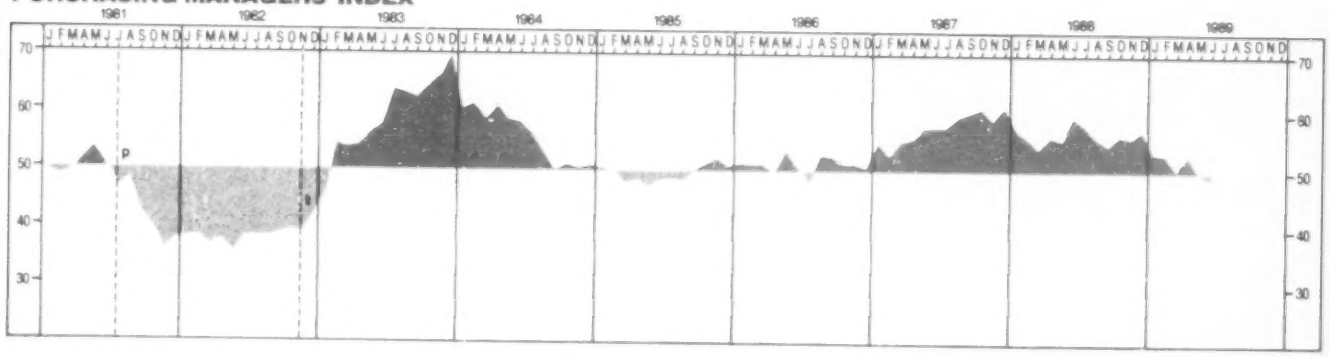
The economy declined in June for the second consecutive month, say the nation's purchasing executives in their latest ***Report On Business.*** **Production** was the only indicator to report an increase in growth. **New Orders** declined in June, for the first time since May 1985, and the New Order index is the lowest since September 1984. Although **Inventories** continued to decline the rate of decline was less than in the previous five months. Some members reported stockpiling in the event of steel-mill work interruptions this summer. In a special question, 30% of members indicated steel was critical to their company's production. Of those 30%, 84% do not expect any work interruption as a consequence of the July 31st contract expiration for several mills which have not yet agreed to terms. However, 65% said they plan to increase inventory prior to July 31st as a hedge against potential steel-work interruptions.

Although the number of members exporting rose to 71% from 69% in May, the rate of growth in **New Export** orders slowed significantly in June. Of those who export, 18% reported better Export Orders, down from 25% in May. The 9% who reported worse Export Orders is up from 5% in May. The seasonally unadjusted index of 54.5% is considerably lower than last month (60.0%).and the lowest since we began this index in January 1988.

Vendor Deliveries were faster for the second consecutive month. The number of commodities reported in short supply was the fewest since October 1987. **Employment** declined for the fifth consecutive month, although the rate of decline was less than in May. For the first time in 34 consecutive months, more purchasing executives reported price decreases than increases. This is the latest in the downward trend in inflation which started in mid-1988.

Robert J. Bretz, C.P.M., chairman of the NAPM Business Survey Committee, and director of materials management at Pitney Bowes, Inc., said, "The total economy continued down the path toward slower growth. The manufacturing economy declined for the second consecutive month as all indicators, except Production, registered declines. The best news is that inflation appears to be slowing at a faster pace than the overall economy."

PURCHASING MANAGERS' INDEX



Purchasing Managers' Index

June	59.2	January '89	53.2
July	57.9	February '89	53.0
August	55.7	March '89	50.4
September	54.7	April '89	53.0
October	56.2	May '89	49.7
November	55.9	June '89	48.8
December	57.3		

The **Purchasing Managers' Index** (PMI) declined to 48.8% in June, down almost a point from 49.7% in May and the lowest since July 1986 (48.0%). This marks the second consecutive decline for this leading indicator, after 33 consecutive months of registering over 50%. A reading below 50 indicates that the economy is generally declining; above 50, that the economy is generally expanding. Bretz added, "The PMI has averaged 51.4% for the first half of 1989. Past experience indicates that if this average were to continue for the second half of 1989 it would be consistent with real GNP growth of about 2.3%. However, the PMI average for the second quarter, 50.5%, appears to be more consistent with real GNP growth closer to 2%. The PMI would have to fall below 44% before signalling negative real GNP."

Data and method of presentation

The *Report on Business* is based on data compiled from monthly replies to questions asked of purchasing executives in over 250 industrial companies. Membership of the Business Survey Committee is diversified geographically, based on value added by state, and by Standard Industrial Classification (SIC) category, based on each industry's contribution to Gross National Product (GNP). Twenty-one industries in 50 states are represented on the committee.

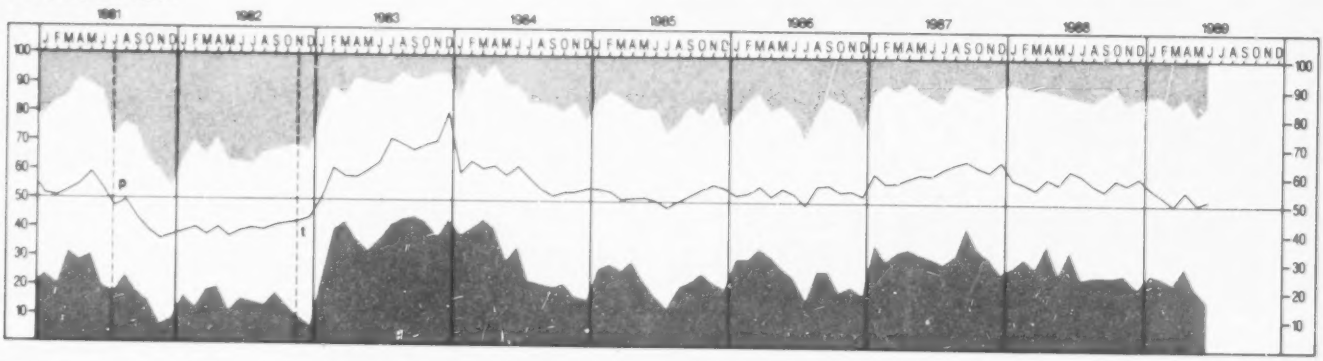
Survey responses reflect the change, if any, in the current month compared to the previous month. For each of the indicators measured (new orders, production, vendor deliveries, inventories, employment and prices), this report shows:

- the percent reporting each response;
- the net difference between the number of responses in the positive economic direction (higher, better — and slower for vendor deliveries) and the negative economic direction (lower, worse — and faster for vendor deliveries);
- the diffusion index.

The charts provide a basis for comparing current data with the historical pattern. The dotted vertical lines on each chart indicate for the period shown the official peak ("p" — July 1981) and trough ("t" — November 1982) of the economy as determined by the National Bureau of Economic Research. The percentage of responses in the positive economic direction are shown in blue, the negative in red, and the same in white. Responses are raw data and are never changed. The diffusion index includes the percent of positive responses, plus one-half of those responding the same (considered positive). The resulting single index number is then seasonally adjusted to allow for the effects of repetitive intra-year variations resulting primarily from normal differences in weather conditions, various institutional arrangements and differences attributable to non-moveable holidays. All seasonal adjustment factors are supplied by the U.S. Department of Commerce and are subject annually to minor changes when conditions warrant them. The Purchasing Managers' Index is a composite index based on the seasonally adjusted diffusion indexes for five of the indicators (new orders, production, vendor deliveries, inventories and employment) with varying weights applied.

Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change and the scope of change. An index reading above 50% indicates that the economy is generally expanding; below 50% generally declining. The distance from 50% is indicative of the strength of the expansion or decline.

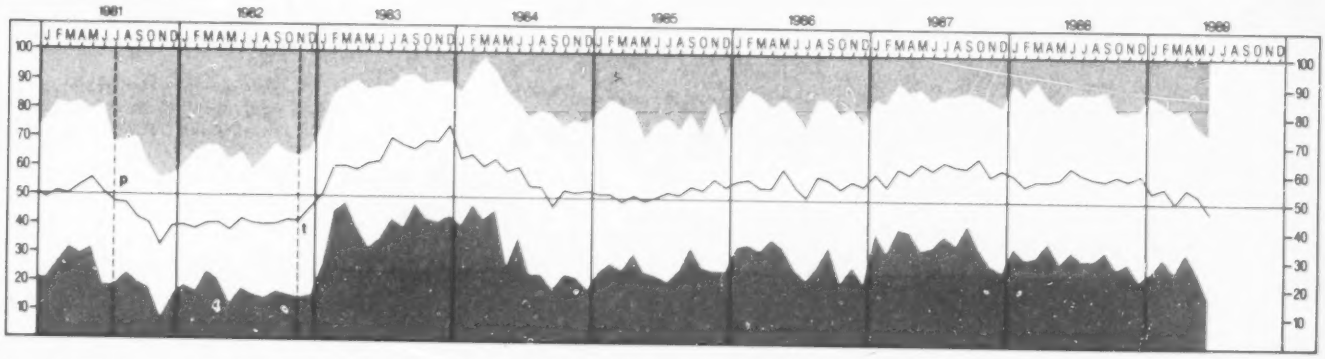
PRODUCTION



Production continued to expand in June for the 35th consecutive month. It remains the only indicator which has not registered a decline over the past few months. The Production index actually rose slightly to 52.4%, up from 51.1% in May.

Production	%Better	%Same	%Worse	Net	Index
June	18	67	15	+ 3	52.4
May	22	59	19	+ 3	51.1
April	30	58	12	+ 18	55.5
March	24	60	16	+ 8	50.7

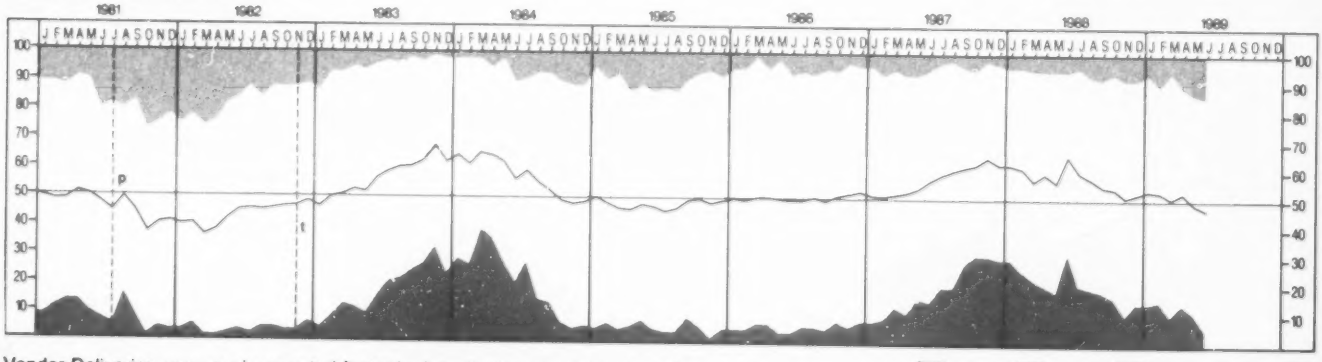
NEW ORDERS



New Orders declined in June, breaking a string of 48 consecutive months of expansion. The New Order index fell significantly to 47.2% from 53.4% in May and is the lowest since September 1984 (also 47.2%). An apparent reason for the sharp drop is the considerable slowing in New Export Orders in June.

New Orders	%Better	%Same	%Worse	Net	Index
June	18	56	26	- 8	47.2
May	27	50	23	+ 4	53.4
April	34	49	17	+ 17	55.3
March	27	55	18	+ 9	50.9

VENDOR DELIVERIES



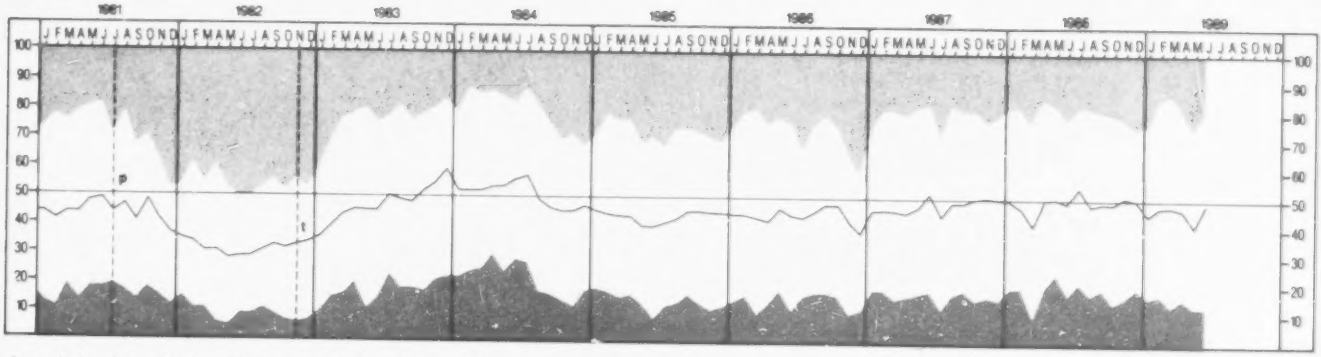
Vendor Deliveries were again reported faster in June for the second consecutive month after 31 consecutive months in which Vendor Deliveries were reported slower. The Vendor Deliveries index fell to 47.5%, down from 49.3% in May, and the lowest since August 1985 (46.6%) for this leading indicator. The number of commodities reported in short supply declined to 10, the fewest since October 1987(9).

Vendor Deliveries	%Slower	%Same	%Faster	Net	Index
June	6	80	14	- 8	47.5
May	12	75	13	- 1	49.3
April	15	74	11	+ 4	53.2
March	11	84	5	+ 6	51.2

IN SHORT SUPPLY:

Castings (7th time in 10 months), **Bleached Paperboard** (12th consecutive month but reported off allocation), **Acrylic Acid** (11th time in 12 months; used in manufacturing plastics), **Caustic Soda/ Soda Ash** (25th consecutive month; used heavily in paper-making, petroleum refining and soap-making), **Freon** (used heavily as a refrigerant and as aerosol propellants), **Sodium Chlorate** (used heavily in paper-making and dyeing), **Titanium Dioxide** (23rd consecutive month; lead-free pigment used as a whitener in coatings, paints, paper and other industrial applications), **Zircon** (3rd consecutive month; used in making glass), **Polyester** (5th consecutive month; reported to be on allocation), **Bearings** (11th consecutive month; a consequence of anti-dumping suits).

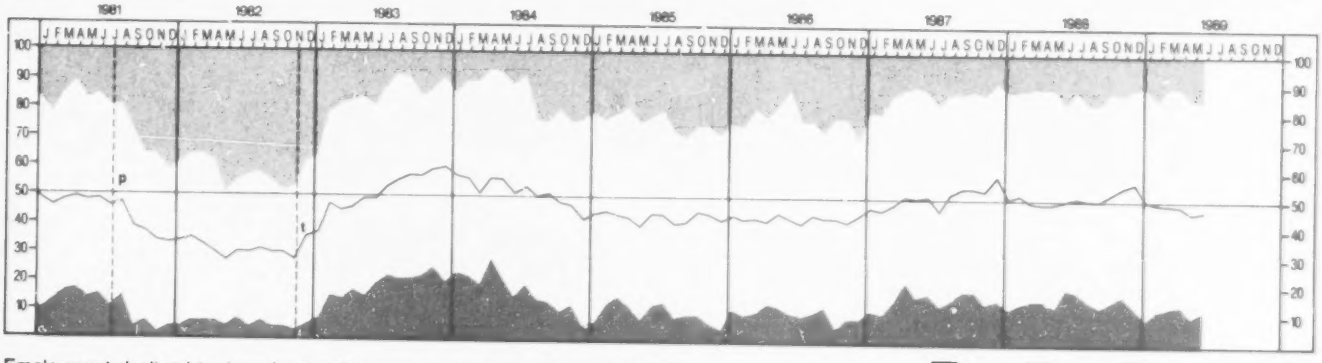
INVENTORIES



Inventories have declined in every month in 1989. This month's decline was not as severe as in May. The Inventories index (49.7%) was up from May (41.9%) and the nearest to growth since December 1988 (50.8%). Some purchasers indicated an increase in inventory from an unexpected slowing in demand in June. Others reported building a slight inventory of steel as a safeguard if some steel suppliers experience work interruptions due to termination of many steel industry labor contracts.

Inventories	%Higher	%Same	%Lower	Net	Index
June	14	68	18	− 4	49.7
May	14	61	25	− 11	41.9
April	17	64	19	− 2	47.4
March	14	73	13	+ 1	48.6

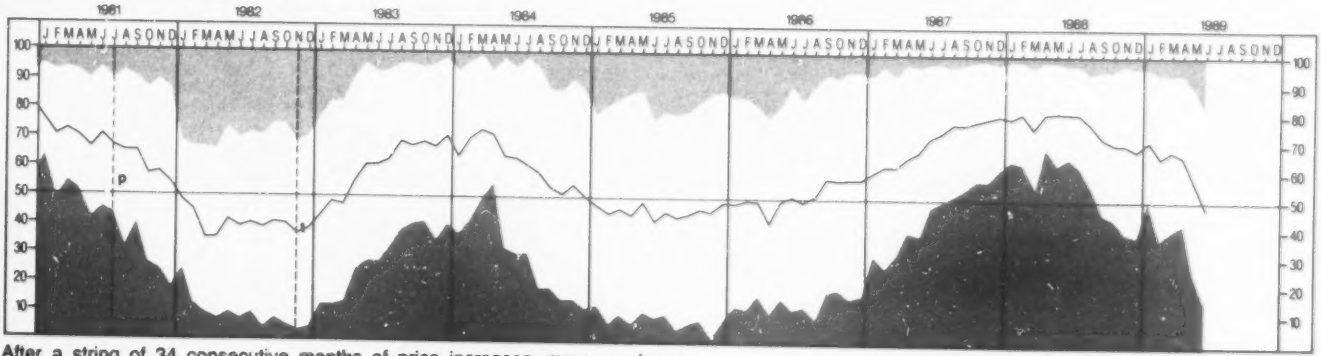
EMPLOYMENT



Employment declined in June for the fifth consecutive month. The Employment index registered 47.4% in June, up a point from 46.4% in May. The slowing in the decline in Employment may have been caused by an increase in temporary summer employees who fill in for vacationing permanent employees.

Employment	%Higher	%Same	%Lower	Net	Index
June	13	72	15	− 2	47.4
May	11	75	14	− 3	46.6
April	15	75	10	+ 5	49.2
March	14	76	10	+ 4	49.4

COMMODITY PRICES



After a string of 34 consecutive months of price increases, more purchasers reported price decreases than increases in June. The Price index plunged for the second consecutive month to 48.5%, down sharply from 57.6% in May and the lowest since April 1986 (42.8%). Mirroring this decline in prices is the decline in the number of commodities reported up in price (6), the fewest since December 1986 (3). Also, 17 commodities were reported lower in price, many of which were only recently reported as increasing in price.

Prices	%Higher	%Same	%Lower	Net	Index
June	16	66	18	− 2	48.5
May	25	65	10	+ 15	57.6
April	43	52	5	+ 38	66.5
March	41	54	5	+ 36	68.3

UP IN PRICE:

Bearings (11th time in 12 months), **Caustic Soda/Soda Ash** (31th consecutive month; used heavily in paper-making, petroleum refining and soap-making), **Glycerine** (used in various ways, especially as a sweetener in confectionaries, cosmetics, soaps and tobacco), **Sugar, Polyester** (7th consecutive month), **Fuel Oil** (7th consecutive month), **Natural Gas**.

DOWN IN PRICE:

Aluminum (3rd consecutive month, after being reported up in price in January for 22nd time in 24 months), **Brass** (reported up in price in March for 2nd time in 4 months), **Copper** (reported up in price in March for 21st time in 25 months), **Nickel** (reported up in price in April for 11th time in 14 months), **Zinc** (2nd consecutive month, after being reported up in price in April for 15th time in 16 months; used heavily in metal alloys and as a protective coating for metal), **Benzine** (used heavily in making medicinal chemicals, dyes, varnishes, lacquers and resins), **Ethylene** (2nd consecutive month; used heavily in making ethylene oxide, plastic resins and glycols), **Formaldehyde, Methanol** (5th time in 6 months; used heavily as a solvent and in synthesizing other chemicals), **Methyl Ethyl Keytone (MEK)** (3rd time in 4 months; used heavily as a chemical solvent in surface coatings and in making resins), **Phenol** (used heavily in making phenolic resins), **Phenolic Resin** (used in making plastic products), **Polyethylene Resin** (3rd consecutive month; used heavily in making packaging materials and paper coatings), **Polystyrene** (2nd consecutive month; used chiefly in making synthetic rubber, plastic resins and plastic), **Styrene** (2nd consecutive month; used chiefly in making synthetic rubber, plastic resins and plastic), **Soybean Oil** (used heavily in processed foods), **Diesel Fuel** (reported up in price in April).

BUYING POLICY

Lead times for Production Materials changed only slightly as purchasers reacted cautiously to improving deliveries and fewer shortages. The number of members reporting lead times of 30 days or less for Production Materials increased imperceptibly to 52%, up from 51% last month. Lead times for Capital Expenditures shortened somewhat. Members reporting lead times in the significant 6 months and longer category for Capital Expenditures declined to 53% in June, down from 55% in May and 56% in April. Lead times for Maintenance, Repair and Operating (MRO) Supplies decreased as the number of members reporting buying hand-to-mouth increased to 41%, up sharply from 37% last month.

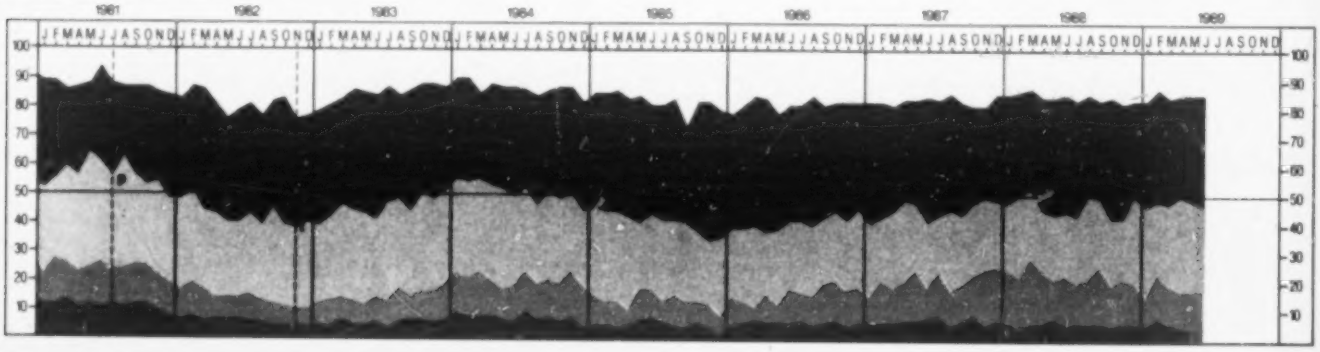
Percent Reporting

Production Materials	Hand to Mouth	30 Days	60 Days	90 Days	6 Mos. and Longer
June	14	38	30	13	5
May	14	37	31	13	5
April	14	35	33	13	5
March	15	37	28	14	6

Capital Expenditures	Hand to Mouth	30 Days	60 Days	90 Days	6 Mos. and Longer
June	13	7	10	17	53
May	13	3	12	17	55
April	13	3	9	19	56
March	11	5	9	21	54

MRO Supplies	Hand to Mouth	30 Days	60 Days	90 Days	6 Mos. and Longer
June	41	44	12	3	0
May	37	47	13	2	1
April	39	42	14	4	1
March	41	46	12	1	0

PRODUCTION MATERIALS



Commodity Report
June, 1989

NON-FERROUS METALS — Prepared by the NAPM Non-Ferrous Metals Committee. Chair: Sharon Sinke, C.P.M., C.L. Frost Inc., Grand Rapids, MI.

COPPER: The first half of 1989 for copper has been a period of uncertainty with many supply interruptions, high levels of consumption and correspondingly high prices. At the same time, interest rates have been rising to cool the economy and are now impacting copper consuming industries such as housing. Major Canadian, Chilean, and American producers have expiring mid-year labor contracts and potential for work stoppages. Worldwide inventories are adequate and slowly growing, with ready availability the norm globally. Aside from potential supply disruptions, stable to decreasing consumption, coupled with rising production and acknowledged costs of $.50–$.70/#, prices should continue the process begun in May, to gradually and steadily decline from recent levels.

LEAD: On June 1, 1989, lead was quoted at $0.37–38/lb. Expect prices to increase incrementally over the next couple months to a high of $0.42 to $0.44/lb. After the first of the year, when demand from battery manufacturers slackens, the price should drop back to the mid to high $0.30's/lb. Present U.S. supplies are tight with most primary and secondary smelters running at capacity. Demand by the battery industry is strong and is expected to remain so through the year-end. Expected new secondary smelting capacity has been delayed, causing demand to exceed supply. LME stocks are 34,000 metric tons lower than one year ago. This reduction, coupled with very strong demand from Asia, will ensure a strong world market through the remainder of 1989.

ZINC: Continued strong demand from consumers, coupled with supply disruptions from three North American producers, forced the U.S. zinc market into near panic in the first quarter. Producer Prices rose from $.75/lb. at the beginning of January to $.95/lb. at the end of February. Traders provided no relief, as their quotes topped $1.00/lb. at one point. During the second quarter, a long anticipated correction has occurred. As of mid-June, the Producer Price stands at $.80/lb. Spot material, which had been nearly impossible to acquire, is starting to reappear. A supply-demand balance has been reached; however, it is quite precarious. Any perceived or actual production loss, such as a labor problem at Noranda, could cause problems with availability and another price spike. Although demand for zinc is expected to flatten in the second half, prices are expected to stay above historical levels. No significant increases in mine or smelter production planned during the rest of 1989, price declines will probably be limited, although availability should continue to improve. A key indicator to watch is auto production, as any cutbacks may signal a slowdown in galvanizing and die-casting.

ENERGY — Prepared by NAPM Energy Committee. Chair, Howard T. Perley, C.P.M., International Paper, Memphis, TN.

PETROLEUM PRODUCTS: Greater demand, U.S. imports, and OPEC's apparent ability to limit production have caused unexpectedly high prices. Though some doubt that OPEC can maintain its production discipline, the supply-demand balance points to firm U.S. product prices.

NATURAL GAS: If you currently buy gas on a month-to-month spot price basis, consider switching to a twelve-month fixed price contract. Take advantage of summer price dips to lock in a firm price and avoid worries next winter. Make sure your contract does not contain a price-renegotiation clause.

ELECTRIC POWER: Many electric utilities are receptive to negotiating individual contracts for industry, and willing to work with industry to assure that the most economical tariffs are applied.

FUSION: The world's scientific community has been excited since the March 23 announcement of a revolutionary fusion energy experiment in Utah. Two chemists reported finding a simple, cheap way to produce fusion energy at room temperature using a beaker of heavy water and a platinum wound palladium rod. They claimed the experiment yielded four times the energy put into it. If the results prove valid, they could lead to a clean, virtually inexhaustible energy supply. But even the most optimistic forecasters feel it would be at least twenty years before this table top model could be scaled-up to commercial applications.

COAL: A new acid rain law in 1989 or 1990 appears more certain. With mandated decreases in SO_2 emissions, the coal industry is facing a spotted future. High sulfur coals are expected to lose 14% of their volume while low sulfur coal volumes could increase 40% by 1995. High sulfur coal prices will remain very soft while compliance coal prices may increase as much as 8% annually. Coal users should be considering long-term contracts with fixed prices for compliance coal, or evaluating the alternative costs of emission controls to take advantage of lower priced high sulfur coals.

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